

Message Text

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ACTION NEA-10

INFO OCT-01 EUR-12 ISO-00 SP-02 USIA-06 AID-05 EB-07
NSC-05 EPG-02 TRSE-00 SS-15 STR-04 OMB-01 CEA-01
CIAE-00 FRB-03 INR-07 NSAE-00 XMB-02 OPIC-03
LAB-04 SIL-01 /091 W
-----050739Z 075324 /21

P R 050640Z JUN 77
FM AMEMBASSY ABU DHABI
TO SECSTATE WASHDC PRIORITY 6178
INFO USDOC WASHDC PRIORITY
AMEMBASSY ATHENS
AMEMBASSY CAIRO
AMCONSUL DHAHRAN
AMEMBASSY DOHA
AMCONSUL ISFAHAN
AMEMBASSY JIDDA
AMEMBASSY KUWAIT
AMEMBASSY LONDON
AMEMBASSY MANAMA
AMEMBASSY MUSCAT
AMCONSUL SHIRAZ
AMEMBASSY TEHRAN

C O N F I D E N T I A L SECTION 1 OF 2 ABU DHABI 1665

USDOC FOR CAGNE

ATHENS FOR RTDO

LONDON FOR KNSOLVING

E.O. 11652: GDS
TAGS : EGEN: ECON
SUBJECT : BUSINESS DOWNTURN IN THE UAE - TEMPORARY BUT JOLTING

REFS: (A) ABU DHABI 870 (NOTAL), (B) ABU DHABI 1585
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(NOTAL), (C) ABU DHABI 1613 (NOTAL), (D) ABU DHABI
1643 (NOTAL)

SUMMARY: ECONOMIC DOWNTURN IS BEGINNING IN UAE.
SEVERAL SECTORS OF ECONOMY WILL BE AFFECTED, BUT
CRUNCH WILL BE MOST SEVERE IN BUILDING CONSTRUCTION
INDUSTRY. AIRGRAM FOLLOWS. END SUMMARY.

1. FULLBLOWN ANALYSIS FOLLOWS IN AIRGRAM, BUT BUILDING DOWNTURN NOTED REF A NOW APPEARS LIKELY TO DEVELOP INTO FULL SCALE RECESSION DUE TO OVERBUILDING AND THE CREDIT SQUEEZE RECENTLY INSTITUTED BY THE UAE CURRENCY BOARD. RENTS ARE BEGINNING TO LEVEL THROUGHOUT THE COUNTRY AND ARE ACTUALLY BEGINNING TO DROP IN DUBAI, RAS-AL-KHAIMAH, AND SHARJAH. LAND PRICES HAVE DROPPED IN THOSE EMIRATES AS WELL. THE RATE OF BUILDING STARTS HAS BEEN OFF SHARPLY IN RECENT MONTHS.

2. BANKS, WHICH HAVE BEEN LESS AND LESS WILLING TO LEND FOR CONSTRUCTION OF NEW BUILDINGS, NOW FLATLY REFUSE TO CONSIDER SUCH LOANS. UAE CURRENCY BOARD'S RECENT ABRUPT IMPOSITION OF NEW REGIME IN BANKING SECTOR WITHIN LAST TWO WEEKS HAS LED TO FURTHER REDUCTION IN SUPPLY OF CREDIT. SUDDENNESS OF THE CURRENCY BOARD'S ACTION HAS SOAKED UP LIQUIDITY AT A TIME WHEN MANY CONTRACTORS AND BANKS WERE STRETCHED VERY THIN. AN AMERICAN CONTRACTOR WORKING IN THE NORTHERN EMIRATES ASSERTS THAT SEVERAL SMALL AND MEDIUM-SIZED CONTRACTING FIRMS THERE HAVE BEEN FORCED INTO BANKRUPTCY. IN ABU DHABI IT HAS BEEN SUSPECTED FOR SEVERAL MONTHS THAT MANY CONTRACTORS WERE FINANCING CURRENT PROJECTS WITH TEN PERCENT ADVANCE PAYMENT FOR ANY NEW WORK THEY COULD SECURE AND THAT THEY WERE THUS DESPERATELY BIDDING NEW WORK BELOW COST. SEVERAL BANKRUPTCIES OF ABU DHABI BUILDING CONTRACTORS SIMULTANEOUS WITH DOWNTURN IN NEW BUILDING STARTS SEEM TO HAVE CONFIRMED

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THIS.

3. SOME BANKS HAVE STRETCHED THEMSELVES VERY THIN AS WELL. MANY OF THOSE WHICH HAVE BEEN HEAVILY INVOLVED IN REAL ESTATE FINANCING MAY SOON FIND THEMSELVES IN DIFFICULTY - ESPECIALLY THOSE WHICH HAVE FINANCED REAL ESTATE LOANS FROM THE SHORT-TERM MONEY MARKETS. TWO BANKS, THE JANATA BANK AND THE AJMAN-ARAB BANK HAVE ALREADY BEEN CLOSED (DETAILS REF B,C,D) AND THEIR DEPOSITORS HAVE YET TO RECEIVE ANY ASSURANCE THAT THEIR MONEY WILL BE PROTECTED. AS A CONSEQUENCE, FAITH IN MANY LOCAL BANKS HAS WEAKENED. RUMORS AROUND THAT OTHER BANKS MAY ALSO BE CLOSED, CONTRIBUTING TO A GENERAL DECLINE IN BUSINESS CONFIDENCE.

4. FINANCING PROBLEMS WERE ALREADY SPREADING TO COMMERCIAL SECTOR AND CURRENCY BOARD ACTION, ALTHOUGH

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C O N F I D E N T I A L FINAL SECTION OF 2 ABU DHABI 1665

USDOC FOR CAGNE

ATHENS FOR RTDO

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NECESSARY AND SALUTARY IN THE LONG RUN, HAS SERVED TO
SPEED PROCESS. SOME BANKERS IN DUBAI REPORT THAT TRADERS
IN INCREASING NUMBERS ARE FAILING TO PAY THEIR LETTERS
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OF CREDIT ON PRESENTATION. BANKS HAVE LET MERCHANTS TAKE

THEIR GOODS UNDER LETTERS OF TRUST PAYING THE BANK WITH FUNDS REALIZED FROM THE SALE OF MERCHANDISE. JANATA BANK'S PROBLEMS WERE COMPOUNDED BY ITS LOSSES ON "LETTER OF TRUST" ON 21,000 TON STEEL SHIPMENT WHICH FINALLY WAS SOLD AT BELOW COST. AN AMERICAN BANKER IN DUBAI PREDICTS "A LARGE NUMBER OF BANKRUPTCIES IN COMING MONTHS".

5. LAISSEZ-FAIRE APPROACH TO BUSINESS HAS LONG BEEN STANDARD OPERATING PROCEDURE IN DUBAI, AND HOW MUCH SHAIKH RASHID WILL DO TO MINIMIZE COMING CRUNCH IS OPEN TO QUESTION. GIVEN RASHID'S HEAVY COMMITMENTS FOR INFRA-STRUCTURAL PROJECTS, HE MIGHT FIND IT DIFFICULT TO DO MUCH, EVEN IF HE WERE SO INCLINED. A NATIONAL BANK OF ABU DHABI OFFICIAL, ON THE OTHER HAND, REFLECTED THE LOCAL CONSENSUS WHEN HE SAID THAT SHAIKH ZAYID WOULD BE VERY LIKELY TO STEP IN TO PREVENT RIPPLE EFFECT FROM CONSTRUCTION INDUSTRY SPREADING TO INTERFERE WITH DEVELOPMENT OBJECTIVES IN ABU DHABI. OF COURSE, THERE IS NO QUESTION THAT ZAYID HAS THE FINANCIAL WHEREWITHAL TO FORESTALL REAL PROBLEMS. UAEG ANNOUNCEMENT JUNE 3 OF A SHARP INCREASE IN CIVIL SERVICE SALARIES SHOWS THAT UAE HAS MEANS TO SUPPORT DEMAND AT ALMOST WHATEVER LEVEL IT CHOOSES.

6. COMMENT: HIGH LEVEL ECONOMIC ACTIVITY IN UAE HAS BEEN GEARED BY REAL DEMAND FOR GOODS AND SERVICES AND CONCOMITANT RESOURCES TO PAY FOR THEM. THUS SETBACK WILL BE TEMPORARY. ANTICIPATED OIL REVENUES IN EXCESS OF EIGHT BILLION DOLLARS THIS YEAR WILL PROVIDE AMPLE GUARANTEE THAT UAE BOOM WILL NOT COLLAPSE. NEVERTHELESS, RECESSION IN THE BUILDING SECTOR WILL HAVE REPERCUSSIONS IN TRADING, BANKING AND REAL ESTATE PARTICULARLY. EXTENT TO WHICH INDIVIDUALS WILL BE PROTECTED FROM EXCESSES OF PAST FEW YEARS WILL DEPEND - AS IN LARGE MEASURE EVERYTHING IN UAE DEPENDS - ON DISPOSITION OF OIL
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REVENUES. IF PAST TRACK RECORD IS USEFUL GUIDE, DUBAI AND SHARJAH WILL SUFFER BECAUSE OF LACK OF PLENTIFUL OIL MONEY TO OFFSET DOWNTURN, WHILE ABU DHABI CAN BE EXPECTED TO WEATHER SHAKEDOWN IN MUCH EASIER FASHION. IMPLICATIONS FOR UAE FEDERAL UNITY ARE SPECULATIVE, BUT PROVOCATIVE. PLAUSIBLE ARGUMENT CAN BE MADE THAT THE WORSE THE DOWNTURN, THE BETTER FOR UNIFICATION OF COUNTRY UNDER ABU DHABI HEGEMONY. IN FACT, HOWEVER, WE DO NOT SEE THE DOWNTURN AS LONG-LASTING OR SEVERE, BUT MORE AS A CORRECTIVE TO BRING BACK SOME REALITY TO A NATION GROWN TOO AT EASE WITH THE SURREAL.
DICKMAN

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